SUMMARY of COOPERATIVE CASES

FARMER COOPERATIVE SERVICE
U. S. DEPARTMENT OF AGRICULTURE
WASHINGTON, D. C.

SUMMARY NO. 63

MARCH 1955

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The comments on cases reviewed herein represent the personal opinion of the author and not necessarily the official views of the Department of Agriculture.

B. A. CARPENTER DECISION AFFIRMED IN CIRCUIT COURT

(Commissioner of I.R. v. B. A. Carpenter, _____F. 2d _____)

In a unanimous opinion, the U. S. Court of Appeals for the Fifth Circuit on March 2, 1955, affirmed the decision of the Tax Court of the United States which was rendered June 15, 1953 (See Summary No. 57, p. 1), holding that revolving fund certificates issued by a farmers' cooperative to B. A. Carpenter did not constitute taxable income to the taxpayer in the year of issue. The Circuit Court rejected as "unsound" the receipt and reinvestment theory advanced by the Commissioner. It did not mention or discuss the cooperative tax cases in reaching its conclusion.

Text of the opinion follows:

> "This appeal is from a decision of the Tax Court, which held that the respondent was not liable for alleged income tax deficiencies asserted to be owing for the fiscal years ending February, 1946, through 1949. The facts are not in dispute, and the only question is whether the respondent must include in his gross income the face amount of revolving fund certificates issued by a farmer cooperative association.
>
> "There was an agreement between Fosgate Growers Cooperative, a farmer cooperative association, exempt under Section 101(12) of the Internal Revenue Code of 1939, and its patrons, whereby the cooperative would sell the produce delivered to it by the patrons and would either return to the patrons the proceeds received for such produce over and above necessary expenses or, at the option of the cooperative, keep that portion of such proceeds necessary to establish and maintain adequate reserves, upon the condition that the cooperative would issue to the patrons a revolving fund certificate in a face amount equal to that patron's share of the retained proceeds. These certificates were redeemable only in the sole discretion of the directors of the cooperative, were non-interest-bearing, were junior to all debts of the cooperative, and could be redeemed only upon written approval of the Columbia Land Bank, the mortgagee of the cooperative. The certificates admittedly had no fair market value when issued to the respondent.

"The Commissioner insists that the revolving fund certificates should be taxable at their face amount, regardless of whether or not they had any fair market value at the time of issuance. The argument advanced by the Commission is that the cooperative was under an obligation to distribute patronage dividends either in cash or certificates, that respondent assented to this arrangement by becoming a patron; and that when the directors have determined to issue the certificate the respondent should be treated as if he had actually received the cash in the amount evidenced by the certificate and reinvested the cash in the cooperative. We think such contentions are unsound.

"It is abundantly clear that the taxpayer's receipt of revolving fund certificates was not the equivalent of the actual receipt of cash, because the certificates had no fair market value. Furthermore, it is obvious that the funds withheld by the cooperative were not subject to the demand of the respondent. The respondent could control neither the amount of the funds that he would ultimately receive nor the time at which he might receive them. These matters were left to the discretion of the cooperative's directors, and even the directors could not pay off the certificates without written consent of the mortgagee. Therefore, the respondent never actually or constructively received or had any right to receive anything but the certificates. It is fundamental in income taxation that, before a cash basis taxpayer may be charged with the receipt of income, he must receive cash or property having a fair market value, or such cash or property must be unqualifiedly subject to his demand. We are of the opinion that the certificates, when issued to the respondent, did not constitute income. Accordingly, the judgment appealed from should be and is AFFIRMED."

PRICE DISCRIMINATION OF PURELY LOCAL NATURE BY INTERSTATE COMPETITOR IS BARRED

(L. L. Moore v. Mead's Fine Bread Co.
348 U.S. 115, 75 S. Ct. 148, 99 L. Ed. 123)

Occasionally reports have been received of a concern engaged in interstate commerce which cuts the price of a product locally so as to injure a local cooperative selling the same type of product. The recent decision of the Supreme Court of the United States in the case cited above should be of interest to any cooperative faced with this type of unfair competition.

The court held in this case that the purely local nature of a baker's operations did not deprive him of his right to bring a Robinson-Patman Act suit for treble damages against an interstate competitor which lowered its bread prices below cost only in the town in which the baker operated.

Moore was engaged in the bakery business at Santa Rosa, New Mexico. Respondent was a corporation in business in Clovis, New Mexico, and was one of several corporations having interlocking directorates which operated in Texas as well as New Mexico. A Texas town was also served from the Clovis plant.

For some months Moore and respondent were in competition in Santa Rosa. There was evidence that, on the threat of Moore to move to another town, the local merchants agreed to purchase his products exclusively. Respondent, labeling that action a boycott, cut the wholesale price of bread in Santa Rosa from 14 cents to 7 cents for a pound loaf and from 21 cents to 11 cents for a pound and a half loaf. The price war continued about eight months and, as a result, Moore was forced to close his business.

After setting forth these facts, the court said:

> "The Court of Appeals reversed the judgment for petitioner on the ground that the injury resulting from the price cutting was to a purely local competitor whose business was in no way related to interstate commerce. 'If competition was lessened or a monopoly created,' said the Court of Appeals, 'it was purely local in its scope and effect and in no way related to or affected interstate commerce.' 208 F. 2d 777, 780.

"Section 2(a) of the Clayton Act, as amended, 15 U.S.C. Sec. 13(a), provides in part:

> "'It shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality, where either or any of the purchases involved in such discrimination are in commerce, where such commodities are sold for use, consumption, or resale within the United States . . . and where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them. . . .'

"Section 3 of the Robinson-Patman Act, 15 U.S.C. Sec. 13a, provides in part:

> "'It shall be unlawful for any person engaged in commerce, in the course of such commerce, . . . to sell . . . goods in any part of the United States at prices lower than those exacted by said person elsewhere in the United States for the purpose of destroying competition, or eliminating a competitor in such part of the United States; or, to sell . . . goods at unreasonably low prices for the purpose of destroying competition or eliminating a competitor.'

"Those sections on their face seem to cover the instant case. Respondent is engaged in commerce, selling bread both locally and interstate. In the course of such business, it made price discriminations, maintaining the price in the interstate transactions and cutting the price of the intrastate sales. The destruction of a competitor was plainly established, as required by the amended Sec. 2(a) of the Clayton Act; and the evidence to support a finding of purpose to eliminate a competitor, as required by Sec. 3 of the Robinson-Patman Act, was ample.

"The Court of Appeals read the antitrust laws as reaching local transactions only where: (1) the local restraint has an effect on the free flow of interstate trade or commerce (e.g., Wickard v. Filburn, 317 U.S. 111); or (2) the restraint on or the

monopoly of local trade is effected through the utilization of interstate mechanisms (e.g., Lorain Journal Co. v. United States, 342 U.S. 143); or (3) local prices are fixed by the use of interstate commercial transactions (e.g., United States v. Frankfort Distilleries, 324 U.S. 293); or (4) the discriminatory sales are to purchasers who compete in interstate commerce (e.g., Corn Products Refining Co. v. Federal Trade Commission, 324 U.S. 726); or (5) interstate commerce is in some other way used to destroy competition or is injured or impaired as a result of unlawful acts.

"We think that the practices in the present case are also included within the scope of the antitrust laws. We have here an interstate industry increasing its domain through outlawed competitive practices. The victim, to be sure, is only a local merchant; and no interstate transactions are used to destroy him. But the beneficiary is an interstate business; the treasury used to finance the warfare is drawn from interstate, as well as local, sources which include not only respondent but also a group of interlocked companies engaged in the same line of business; and the prices on the interstate sales, both by respondent and by the other Mead companies, are kept high while the local prices are lowered. If this method of competition were approved, the pattern for growth of monopoly would be simple. As long as the price warfare was strictly intrastate, interstate business could grow and expand with impunity at the expense of local merchants. The competitive advantage would then be with the interstate combines, not by reason of their skills or efficiency but because of their strength and ability to wage price wars. The profits made in interstate activities would underwrite the losses of local price-cutting campaigns. No instrumentality of interstate commerce would be used to destroy the local merchant and expand the domain of the combine. But the opportunities afforded by interstate commerce would be employed to injure local trade. Congress, as guardian of the Commerce Clause, certainly has power to say that those advantages shall not attach to the privilege of doing an interstate business.

"This type of price cutting was held to be 'foreign to any legitimate commercial competition' even prior to the Robinson-Patman Act. See Porto Rican American Tobacco Co. v. American Tobacco Co., 30 F. 2d 234, 237. It seems plain to us that Congress went at least that far in the Robinson-Patman Act. As we have shown, the facts charged and found read upon the words of the statute. And the history of the Act shows it was

designed to have the reach now claimed for it by petitioner. Congressman Utterback, manager of the bill in the House, included this type of case in the price cutting that he claimed was outlawed:

> "'Where, however, a manufacturer sells to customers both within the State and beyond the State, he may not favor either to the disadvantage of the other; he may not use the privilege of interstate commerce to the injury of his local trade, nor may he favor his local trade to the injury of his interstate trade. The Federal power to regulate interstate commerce is the power both to limit its employment to the injury of business within the State, and to protect interstate commerce itself from injury by influences within the State.' 80 Cong. Rec. 9417.

"It is, we think, clear that Congress by the Clayton Act and Robinson-Patman Act barred the use of interstate business to destroy local business, outlawing the price cutting employed by respondent."

CORRECTION ON FORM 990-C

Farmers' cooperative marketing and purchasing associations qualifying for "exemption" under the Internal Revenue Code are required to file a return on Treasury Department Form 990-C. In item 15 of Schedule M of this form for 1954 is a reference to item 31 on page 1 of the form. This reference is in error and should read "item 33, page 1," according to informal advice from Internal Revenue Service.

FTC COMPLAINT AGAINST WILSON TOBACCO MARKET

(In the matter of Wilson Tobacco Board of Trade, Inc., et al.--
Docket No. 6262)

A hearing was held in March, 1955, on the complaint in the case identified above, which the Federal Trade Commission filed on November 9, 1954, against the Wilson Tobacco Board of Trade, Inc., and its members composed of corporations, partnerships and individuals, including warehousemen, who are generally engaged in either selling, buying, rehandling, or otherwise dealing in leaf tobacco. Included among the nineteen warehouses operating on the Wilson market is the Growers Cooperative Warehouse, Inc.

The complaint charged, among other things, that:

> "PARAGRAPH EIGHT: Respondents, acting between and among themselves and also through and by means of respondent Board and respondent Warehouse Association, for a number of years last past, and particularly since about 1948, and continuing to the present time, have, by means of agreements and understandings between and among themselves and by other means and methods, conspired and combined, together and with others, and have united in and pursued a planned common course of action, to adopt, carry out, and maintain, and have adopted, carried out, and maintained, in commerce between and among the several States of the United States and in the District of Columbia and with foreign countries, an undue and unreasonable hindrance, restriction, suppression, and prevention of the establishment and operation of market facilities and market opportunities and competition in the purchase and sale of leaf tobacco on the Wilson Tobacco market.
>
> "PARAGRAPH NINE: Pursuant to, and in furtherance and effectuation of, the aforesaid agreements and planned common course of action, respondents have done and performed the following things:
>
> > "(1) They have adopted and used a policy and practice of restricting, preventing, and foreclosing persons, firms and corporations from engaging in the business of buying and selling tobacco on the Wilson market.

"(2) They have adopted a policy to discourage and prevent, and acted thereunder for the purpose and with the effect of discouraging and preventing, persons, firms and corporations from erecting, building, or operating any new auction warehouse in or near the Wilson tobacco market area.

"(3) They have adopted a policy to discourage and prevent, and acted thereunder for the purpose and with the effect of discouraging and preventing persons, firms and corporations from expanding their present tobacco auction warehouse facilities in the Wilson tobacco market.

"(4) Respondent members of respondent Warehouse Association formulated, agreed upon, and adopted a resolution providing for a change in the method or system of allocating selling time to the Warehouse Members of respondent Warehouse Association.

"(5) Respondents, acting by and through respondent Board, agreed upon, adopted, and put into effect the aforesaid agreement which had been formulated, agreed upon, and adopted by respondent members of respondent Warehouse Association, providing for a change in the method or system of allocating selling time on the Wilson tobacco market.

"(a) Prior to the time of the change in the method or system of allocating selling time as herein alleged, there was in effect a method or system, known and described as the Floor Space System, of allocating selling time to each of the warehouse operating members of the respondent Board on the Wilson tobacco market, which provided for an allocation of an amount of selling time to each such member in the same proportion to the total selling time available on said market as the said member's warehouse floor space had to the total combined warehouse floor space of all said members.

"(b) The method or system of allocating selling time on the Wilson tobacco market provided for in the aforesaid and challenged agreement, combination,

conspiracy, and planned common course of action by respondents is generally known and described as the Performance System. According to the agreement of the respondents, this system is to run for a minimum of five years from 1952 and provides, among other things, that the selling time available to any Warehouse Member of respondent Board on the Wilson tobacco market during a given selling season shall be limited, determined, and governed by the record of his sales of tobacco on that market for the previous year. The allocation of the selling time on the Wilson tobacco market to each Warehouse Member of respondent Board now is limited and restricted during a given selling season to a certain percent of the total selling time available to all of such said members. The said percentage is determined, controlled and limited by the percent of the total sales recorded as having been made on the Wilson tobacco market by such member during the previous year.

"(6) They have agreed to limit, and have limited, the amount of tobacco that may be offered and sold by any Warehouse Member of respondent Board for resale on the Wilson tobacco market during any given selling season, to 6.8 percent of the total net sales of such member during the preceding year.

"(7) They have required, pursuant to collective agreement among respondent members of respondent Warehouse Association, that any Warehouse Member refrain from renting or leasing any part of his warehouse except as, and upon the terms, approved by respondent Warehouse Association, and then only upon the condition and understanding that such member pay over to respondent Warehouse Association the rents, monies, and benefits he received from such rentals and leases.

"PARAGRAPH TEN: Each of the respondents herein has directly or indirectly participated in, approved, or adopted the aforesaid agreements, understandings and planned common course of action and the acts and practices done in furtherance of and pursuant thereto.

"PARAGRAPH ELEVEN: The aforesaid agreements, combination, conspiracy, planned common course of action, policies, acts, and practices of the respondents, as hereinbefore alleged, each and all operated to prevent a substantial volume of tobacco from being

sold or purchased by persons, firms and corporations who sought to compete in the market operations of the Wilson tobacco market, and thereby unduly and unreasonably hindered, restricted, suppressed, and prevented competition in the sale and purchase of tobacco on the Wilson tobacco market. Among the specific effects in that respect are the following:

"(1) Persons, firms, and corporations seeking to erect, expand, and use tobacco warehouse facilities in market operations on the Wilson tobacco market were prevented from doing so.

"(2) Persons, firms, and corporations as potential competitors of respondents have been discouraged, persuaded and prevented from further consideration of engaging in competition with respondents on the Wilson tobacco market in the purchase and sale of tobacco.

"(3) Farmers who have only small quantities of tobacco that they can offer for sale on the Wilson tobacco market on any given day have been obstructed and prevented from having their offers considered and acted upon by respondent Warehouse Members of respondent Board.

"(4) Persons, firms and corporations engaged in the buying and selling of tobacco have been foreclosed and prevented from reselling tobacco on the Wilson tobacco market, despite the fact that those who have thus been foreclosed in that respect were otherwise accepted as members of respondent Board.

"(5) Respondents have acquired control of such nature and to such an extent over the purchase and sale of tobacco on the Wilson tobacco market that it has created, and threatens to perpetuate, in them a monopoly in the business of buying and selling tobacco on that market."

RECENT INTERNAL REVENUE SERVICE RULINGS OF INTEREST TO COOPERATIVES

1. Determination of whether patronage allocation which becomes worthless is capital loss or bad debt. (Rev. Rul. 55-66; I.R.B. 1955-6, 15)

"Allocations to patrons in document form issued by a cooperative association in accordance with a preexisting agreement may take the form of certificates denoting an investment in the capital of the cooperative or of certificates of indebtedness of the cooperative. In such cases, it is considered that the patron has in effect received in money the face amount of the document and has either reinvested that amount in the capital of the association or allowed the association the use thereof. See Rev. Rul. 54-10, C.B. 1954-1,24. The bylaws usually disclose the nature of the relationship between the association and its patrons, and hence, whether there has been an investment in capital of or a loan to the association. This relationship is reflected in the type of instrument which a patron receives. By showing whether there has been an investment in capital or a loan, the instrument will indicate whether a loss due to worthlessness upon dissolution or insolvency, of the cooperative which issued it, may be treated as a capital loss or as a bad debt."

2. Exclusion of patronage dividends by farmers' organization not having "cooperative" in the name. (Rev. Rul 55-26; I.R.B. 1955-3, 64)

"Farmers' cooperative marketing and purchasing associations, whose bylaws set forth a definite pre-existing obligation of the association to make distribution to patrons of a portion of the net profits as patronage dividends, may have such dividends excluded from income for Federal income tax purposes regardless of whether the corporate name contains the word 'cooperative.'"

3. Information returns on dividend payments by NFLAs and PCAs

For calendar years after 1953, national farm loan associations and production credit associations will not be required to file information returns on dividend payments of less than $100. (Revised section 39.148(a)-1(b) of Regulations 118; T.D. 6113, approved November 24, 1954)